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IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

COIT INDEPENDENCE JOINT VENTURE,
Petitioner,
v.
FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION,
AS RECEIVER FOR FIRSTSOUTH, F.A.,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF AMICUS CURIAE NATIONAL COUNCIL OF SAVINGS INSTITUTIONS IN SUPPORT OF RESPONDENT

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BRIEF OF AMICUS CURIAE NATIONAL COUNCIL OF SAVINGS INSTITUTIONS IN SUPPORT OF RESPONDENT

INTEREST OF AMICUS CURIAE

The National Council of Savings Institutions ("National Council") is a national trade association of federally chartered and state chartered savings and loan associations and savings banks. Member institutions number approximately 500, with assets in excess of $550 billion. As a trade association, the National Council offers its members a platform for addressing their concerns to Congress and to the regulators, as well as providing a variety of educational programs and publications. The National Council has been permitted to inter-

vene as *amicus curiae* in previous legal actions affecting its members.[1]

Although no specific statistics are available, our member institutions are clearly affected by the regulatory agencies' procedures for bringing claims against receivers. Whatever the amount of current claims of National Council members against insolvent institutions, such claims will increase as more institutions are placed into receivership. Member institutions can become creditors of insolvent institutions through a variety of transactions. Loan participations are the most frequent source of these claims, but other possibilities include sales of branches or receivables, real property leases, and purchases of debt securities.

The National Council seeks intervention as *amicus curiae* because it believes that the interests of its members are best served by securing their access to the administrative procedures established by the Federal Home Loan Bank Board ("Bank Board") for settlement of claims against receivers. These procedures offer claimants a full and fair opportunity to establish their claims, at a much lower cost in time and expenses than a court proceeding. In our view, if claimants are allowed to choose between a judicial trial and the administrative process, a few litigious claimants could delay the liquidation and payout of claims by a receiver for years. Likewise, if claimants are given the option of a full-blown trial in court, after exhaustion of administrative remedies, the effectiveness of the administrative procedure will be greatly impaired, to the ultimate delay, detriment and expense of a great many creditors.

Many of our members' deposits are insured by the Federal Savings and Loan Insurance Corporation ("FSLIC") and they have a direct interest in the sound-

[1] Counsel for Petitioner and for Respondent have consented to the filing of this Brief. Their letters of consent are on file with the Clerk of the Court.

ness of the FSLIC insurance fund. They share with Amici Federal Home Loan Banks the concerns for the health of the savings and loan industry. Even those savings bank members whose deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") have stated emphatically their wish to preserve the FSLIC as an insurer for thrift deposits. We agree with the sentiments expressed by the United States League of Savings Institutions ("Amicus League") when it "congratulate[d] the [Bank] Board in its efforts to clarify and streamline its regulations governing the appointment and powers of conservators and receivers" and went on to note that "it is important to give the FSLIC the broad power it needs to protect the FSLIC fund." Comments of the Amicus League on proposed FSLIC receivership claims regulations, January 30, 1986 (attached as Appendix A).[2] Although the Bank Board's statutory powers are far from unlimited, they do not have to be construed broadly to find authority to determine creditor claims against institutions for which the Bank Board has appointed the FSLIC receiver.

SUMMARY OF ARGUMENT

The Bank Board relies on a three-part statutory structure as authority for establishing its claims procedures requiring exhaustion of administrative remedies:

—12 U.S.C. § 1729(d) authorizes FSLIC as receiver to adjudicate claims;

—12 U.S.C. § 1464(d)(11) authorizes enactment of rules governing resolution of claims; and

—12 U.S.C. § 1464(d)(6)(C) precludes courts from restraining or affecting the receivership.

To allow courts throughout the country to consider claims against a single receivership could result in chaos in the liquidation process. A central consistent source for

[2] The proposed regulations were published at 50 Fed. Reg. 48970 (1985).

determining claims exists at the receivership level in each instance with review at the Bank Board, where expertise can be applied and consistency achieved—not only in individual receiverships but also from one receivership to another.

The FDIC statute specifically provides for optional adjudication in court. Because the FSLIC authority was enacted later without such provisions, we conclude Congress intended a different system. The venue provision in the FDIC's statute also differs considerably from FSLIC's by limiting claims to courts where the bank's principal office is located. 12 U.S.C. § 94. By providing expressly for judicial adjudications for the FDIC and by leaving out the venue protection for the FSLIC, Congress deliberately chose a different system for the FSLIC.

We find no merit to the Constitutional claims proferred by Petitioner. They are premature because Petitioner has not yet suffered any direct injury from the requirement to pursue the administrative process. No Article III violation occurs because FSLIC is not exercising powers of a court; the claims process is an integral part of a larger regulatory scheme. There is no right to jury trial where Congress validly delegates authority to determine administrative matters. Furthermore, equitable issues, such as claims to settle a bankrupt estate, do not give rise to a right to jury trial.

The FSLIC's dual role of determining claims while also having an interest in the final distribution is not unique in administrative law. Courts have repeatedly held in due process challenges that agencies are entitled to a presumption of fair procedures.

In view of the savings in permitting Bank Board review—both for the claimants and for FSLIC—we support this opportunity for an administrative remedy. Complainants who believe they have been treated improperly may pursue judicial review.

ARGUMENT

I. FSLIC and the Bank Board Have Statutory Authority to Determine Receivership Claims.

The Bankruptcy Code expressly exempts insolvent banking institutions, including savings and loans, from the debtors it reaches. 11 U.S.C. § 109(b)(2). They "are excluded from liquidation under the bankruptcy laws because they are bodies for which alternative provision is made for their liquidation under various State or Federal regulatory laws." S. Rep. No. 95-989, 95th Cong., 2d Sess. 31, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 5817. The question thus presented is, what "regulatory laws" provide for liquidation of federally chartered savings and loan associations? Congress provided initially for the liquidation of these institutions in Section 5(d) of the Home Owners' Loan Act ("HOLA"), Pub. L. 73-43, § 5(d), 48 Stat. 128; and in Section 503 of the Housing Act of 1954, Pub. L. No. 560, § 503, 68 Stat. 634, codified as amended at 12 U.S.C. § 1464 (d)(11). The original version of the HOLA provided simply that the Bank Board should have power to make rules and regulations for the liquidation of federally chartered thrifts.

The Bank Board, as early as 1941, published regulations providing for presentation of proofs to, and allowance and disallowance of claims by, FSLIC, as receiver, with review at the Bank Board. *See* 6 Fed. Reg. 4413 (1941). Those regulations, as amended provide:

> The receiver shall allow any claim seasonably received and *proved to its satisfaction.* The receiver may wholly or partly disallow any creditor claim or claim of security, preference, or priority not so proved, and shall notify the claimant of the disallowance and the reason therefor. * * * Unless, within 30 days after notice is mailed, the claimant files a written request for payment regardless of the disallowance, disallowance shall be final, except as the Board may otherwise determine.

12 C.F.R. § 549.4(b) (1988) (emphasis added).[3]

It has long been recognized by this Court that the power to "[a]llow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates," (Bankruptcy Act of 1898, § 2(a)(2), *formerly codified at* 11 U.S.C. § 11(a)(2) (repealed 1978)), constitutes the power to "adjudicate" those claims. *Katchen v. Landy*, 382 U.S. 323, 329 (1966) quoting *Lesser v. Gray*, 236 U.S. 70, 74 (1915) and *Gardner v. New Jersey*, 329 U.S. 565, 574 (1947). The Seventh Circuit in *Lyons Savings and Loan Ass'n v. Westside Banccorporation, Inc.*, 828 F.2d 387, 392 (7th Cir. 1987), noted:

> Congress has made several amendments to the statutory framework over the course of the past thirty years, . . . but has never limited the FSLIC's authority to adjudicate claims.

Similarly, the Fifth Circuit in *North Mississippi Savings and Loan Ass'n v. Hudspeth*, 756 F.2d 1096, 1102 n.2 (5th Cir. 1985), *cert. denied*, 474 U.S. 1054 (1986), found that the regulations are evidence that adjudication is a receivership function in FSLIC receiverships.[4] Both these circuits plainly view FSLIC's statutory and regulatory scheme as granting authority to "decide" or "adjudicate" a claim with some finality.[5]

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[3] The Bank Board has published detailed interim receivership claims procedures, 53 Fed. Reg. 13105 (1988), which are to remain in effect until finalization of the Bank Board's proposed regulations, 53 Fed. Reg. 21474 (1988).

[4] The Fifth Circuit has reaffirmed *Hudspeth* in *Red Fox Industries, Inc. v. FSLIC*, 832 F.2d 340 (5th Cir. 1987); *FSLIC v. Bonfanti*, 826 F.2d 1391 (5th Cir. 1987), *petition for cert filed*, 56 U.S.L.W. 3165 (U.S. Aug. 5, 1987) (No. 87-255); and *Chupik Corp. v. FSLIC*, 790 F.2d 1269 (5th Cir. 1986).

[5] The Ninth Circuit, however, viewed this issue as its primary difference with the Fifth and Seventh Circuits, finding that the claims process was not deciding claims, but rather whether to contest them. *See Morrison-Knudsen Co., Inc. v. CHG Int'l, Inc.*, 811 F.2d 1209, 1218 (9th Cir. 1987), *petition for cert. filed sub nom. FSLIC v. Stevenson Associates*, —— U.S. —— 56 U.S.L.W. 3249 (U.S. Sept. 17, 1987) (No. 87-451).

In 1954, Congress amended the HOLA to provide expressly that the Bank Board has authority to make rules and regulations for "associations in conservatorship and receivership, and for the conduct of conservatorships and receiverships. . . ." 12 U.S.C. § 1464(d)(11). Congress in 1966 again amended the HOLA to state its intent that the Bank Board be able to conduct liquidations free from interference by the courts:

> Except as otherwise provided in this subsection, no court may take any action for or toward the removal of any conservator or receiver, or, except at the instance of the Board, restrain or affect the exercise of powers or functions of a conservator or receiver.

12 U.S.C. § 1464(d)(6)(C).

The Bank Board, consistent with this Court's ruling in *Katchen*, has consistently interpreted its regulations as providing FSLIC authority to adjudicate claims in the first instance without interference or parallel proceedings in the courts.[6] This procedure is consistent with all other business liquidation systems of which we are aware. All such schemes provide for adjudication of creditor claims in a single forum; many provide that initial claims determinations are to be made by an administrative or court-appointed official. *See* discussion *infra pp.* 11-15. The Bank Board's interpretation, which is clearly not "arbitrary, capricious, or manifestly contrary to the statute," is entitled to great weight. *Chevron U.S.A. Inc. v. NRDC, Inc.*, 467 U.S. 837, 844 (1984); *see also FDIC v. Philadelphia Gear Corp.*, 476 U.S. 426, 438-439 (1986) (FDIC's interpretation of statutory scheme it is entrusted to administer is entitled

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[6] *See Community Federal Savings & Loan Ass'n v. Fields*, 128 F.2d 705, 706 (8th Cir. 1942) (FSLIC argued that failure to file claim barred suit).

to "considerable weight"); *Ford Motor Credit Co. v. Milhollin*, 444 U.S. 555, 566 (1980) (agency interpretation is entitled to "considerable respect").

No brief in this Court nor decision below seriously suggests that FSLIC determination of claims could not reasonably be viewed as furthering the purposes of the HOLA and the National Housing Act ("NHA"). 12 U.S.C. § 1701 *et seq.* Those purposes include liquidation of federal thrifts in "an orderly manner," 12 U.S.C. § 1729(c)(3)(B), and filling the gap left in the Bankruptcy Code for the adjudication of creditor claims against FSLIC, 11 U.S.C. § 109(b)(2).

Congress has never indicated any intent to withhold authority from the Bank Board to make rules for determination of creditor claims—one of the most basic and important liquidation functions. *See FSLIC v. Urquhart*, PCA 86-04294 WEA, slip op. at 4 (N.D. Fla. Apr. 7, 1987) (attached as Appendix B) ("had Congress intended to withhold that authority it would have expressly done so"). To find the Bank Board deprived of power to make rules for this essential function would increase greatly the cost of administering FSLIC receiverships and extend by years the time required to pay out to creditors of failed thrifts the billions of dollars in assets tied up in those receiverships. This result, which is plainly contrary to the purposes of the Bank Board's and FSLIC's enabling statutes, should not therefore be countenanced by this Court. *See Commissioner of Internal Revenue v. Engle*, 464 U.S. 206, 217 (1984); *United States v. Bornstein*, 423 U.S. 303, 314-315 (1976).

The breadth of the Bank Board's rulemaking authority was recently reemphasized by this Court. In *Fidelity Federal Savings and Loan Ass'n v. de la Cuesta*, 458 U.S. 141 (1982), the Court construed a companion section of the HOLA to give the Bank Board "plenary" powers to make rules for the *operation* of federal thrifts. The Court held "it would have been difficult for Congress

to give the Bank Board a broader mandate." *de la Cuesta*, 458 U.S. at 161, quoting *Glendale Federal Savings and Loan Ass'n v. Fox*, 459 F.Supp. 903, 910 (C.D. Cal. 1978). There is no reason to give the agency's liquidation powers a narrower reading.

II. FSLIC's Authority to Adjudicate Claims Is Subject to Review in the Courts Only Under the Administrative Procedure Act.

The National Council concurs with the views of the Bank Board that claims determinations, like other receivership functions, are ultimately subject to judicial review under the Administrative Procedure Act, 5 U.S.C. §§ 701-06 ("APA"). *See American Savings and Loan Ass'n v. FSLIC*, No. 86-689, Brief for the Respondent in Opposition at 7; *Hudspeth v. North Mississippi Savings and Loan Ass'n.*, No. 85-294, Brief for the Respondents in Opposition at 7.

The courts are expressly prohibited from restraining or even affecting the "exercise of powers or functions of a . . . receiver" appointed by the Bank Board. 12 U.S.C. § 1464(d)(6)(C). The NHA grants the Bank Board exclusive authority to supervise the activities of FSLIC and receiver. 12 U.S.C. § 1729(d). Court jurisdiction to adjudicate claims interferes with both the FSLIC's function of claims adjudication and the Bank Board's exclusive authority to supervise and regulate that function. Accordingly, the courts lack jurisdiction to entertain suits against FSLIC as receiver—they are specifically barred from doing so by statute.[7]

Because no role is provided for the courts in FSLIC's receivership statutes, both the Fifth and the Seventh

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[7] Even if the requirement were for nothing more than submission of claims for review and determinations as to whether disputes exist, no case or controversy with the receiver ripens until that procedure is exhausted. In this sense, the exhaustion requirement wold operate much as it does in the Federal Tort Claims Act. 28 U.S.C. § 2675.

Circuits have determined that the only statutory authority for judicial involvement in the claims process is under the APA, 5 U.S.C. § 706. *See Lyons Savings & Loan Ass'n*, 828 F.2d at 395; *Hudspeth*, 756 F.2d at 1103. The APA provides for judicial review of final agency actions on a *de novo* basis as to issues of law, but provides for review on the record of legal determinations and deference to factual findings of the agency. 5 U.S.C. § 706.

In our view, the Ninth Circuit arrived too quickly at the conclusion that courts should have *de novo* jurisdiction to entertain lawsuits against FSLIC receiverships. There is no indication in the HOLA or the NHA that the courts were intended to take such a direct role in deciding whether claims against an insolvent federal thrift should be paid. Moreover, common sense indicates that the agency should not, after it has provided an elaborate two-tier adjudicatory scheme, clearly designed to protect the rights of claimants, be required to attend court in *de novo* proceedings. Such a system would threaten additional delays and, as explained *infra* pp. 11-12, would be quite different from other liquidation schemes. In interpreting the HOLA and the NHA, the Court should choose an interpretation that furthers the purposes of the statute. *Engle*, 464 U.S. 217; *Bornstein*, 423 U.S. at 314-315. Plainly, *de novo* proceedings would not do so.

Further support for deferential review of the agency's decision to disallow claims can be found in recent amendments to the Federal Credit Union Act, by which Congress granted the National Credit Union Administration ("NCUA") authority to adjudicate claims against credit unions in liquidation. 12 U.S.C. § 1787(a)(1)(B). In explaining the amendments, the Senate Report stated that expeditious liquidation serves "to achieve minimal disruption to the financial system." S. Rep. No. 100-19, 100th Cong., 1st Sess. 25, *reprinted in* 8 U.S. Cong. & Admin. News 489, 515 (Oct. 1987).

III. Other Statutory Receiverships Systems Support the Bank Board's Interpretation of Its Statutory Scheme.

Three statutory provisions are relied upon by the Bank Board as authority for administrative claims determinations: 12 U.S.C. § 1464(d)(11) (authorizes enactment of rules governing liquidations and conduct of receiverships); 12 U.S.C. § 1729(d) (authorizes FSLIC as receiver to compromise claims and do all things necessary in connection therewith); and 12 U.S.C. § 1464(d)(6)(C) (precludes courts from "restrain[ing]" or "affect[ing]" the receivership). In order to understand how these provisions affect the claims process, the history of treatment of banking institutions in liquidations is relevant.

Prior to 1933 there were no federally chartered thrifts. There had, however, developed a form of receivership applicable to bankrupt financial institutions—statutory receiverships were largely replacing the traditional "equitable" or court-directed receiverships. The legislatures had come to recognize "that the urgent and delicate issues involved in a bank closure, affecting as they do not only large sums of money, but the credit and assets of its depositors, both small and large, are all matters ill suited for lengthy court hearings." *State ex rel. Arnold v. Egnor*, 275 S.E.2d 15, 21 (W. Va. 1981).

Statutory receiverships placed in question the role of the courts that would otherwise have retained control over the receivership. *In re Union Bank of Brooklyn*, 176 A.D. 477, 163 N.Y.S. 485 (1917) (receivership decisions of the New York Superintendent of Banks were not automatically subject to judicial proceedings). Courts recognized that where the legislature had vested statutory powers in an agency, it was not for them to contest the exercise of those powers. Although review for abuse of power was generally available, discretionary actions of the receiver could not be modified in court. *United States v. Knox*, 102 U.S. 442, 445 (1880). Contrary to

the traditional plenary powers of the courts in an equitable receivership, in a statutory receivership the legislature determines if, when, and under what circumstances decisions made by the receiver may be subject to court review. *See Wm. Filene's Sons Co. v. Weed*, 245 U.S. 597, 602 (1918) ("When a statutory [receivership] system is administered, the only question for the courts is what the statutes prescribe").

By 1934 when Congress created FSLIC, 23 states had enacted purely statutory liquidation schemes for insolvent building and loan associations and another six provided for judicial appointment of receivers, but gave those receivers a level of freedom from court interference similar to that of purely statutory receivers. Note, *Statutory Control Over the Dissolution of Building and Loan Associations*, 35 Colum. L. Rev. 265, 267 n.20 and n.21 (1935). It is not surprising then that Congress did not provide for judicial determination of claims. The principle of limited, deferential judicial review with regard to statutory receiverships was well established long before the enactment of federal thrift receiverships in the NHA. *See* 12 U.S.C. § 1729(b)(1)(A). It is reasonable to interpret this history in support of the Bank Board's authority under 12 U.S.C. § 1464(d)(6)(C) to establish a regulatory claims procedure to resolve claims against the receiver and subject only to APA review in the courts.[8]

[8] At least one state system provides expressly for administrative determination of claims subject only to deferential review under the state Administrative Procedure Act in the courts. W. Va. Code §§ 31A-7-13, 31A-7-14, 31A-7-15. Virtually all state systems provide for consolidation of claims in a single forum, but many state laws are vague about the standard of review of the receivers' decisions to disallow. *See, e.g.*, N.C. Gen. Stat. §§ 54B-70 (1981) (administrator authorized to promulgate regulations governing payment of claims and has authority to "pass on" claims); *Citizens State Bank of Noblesville v. Wright*, 19 N.E.2d 258, 262 (S. Ct. Ind. 1939) (determination by Attorney General and State Auditor has same effect as court order).

IV. Other Federal Banking Statutes Confirm FSLIC's Exclusive Authority to Adjudicate Claims.

When the FDIC is appointed by the Comptroller of the Currency ("Comptroller") to act as a receiver for a closed national bank, the two-tier review structure created by the Bank Board is not available. The more limited nature of the FDIC's claims process results from the National Bank Act's ("NBA") explicit provision that claims may be determined administratively by the Comptroller or by seeking adjudication in court. *See* 12 U.S.C. § 194.[9] Because this statute was in existence prior to the Bank Board's statutes, it might be expected that Congress would provide a similar right to judicial adjudication in the Bank Board and FSLIC statutes. It chose not to however, instead delegating to the Bank Board broad authority to make rules for liquidations, including, it seems logical to conclude, rules for determination of creditor claims. Furthermore, FSLIC's power to settle or release claims subject only to the regulation of the Bank Board has no parallel provision in the FDIC legislation. The NBA differs from the FSLIC system in another important detail—venue of all claims against FDIC as receiver is exclusive in one of the courts (state or federal) where the bank's principal office is located. *See* 12 U.S.C. § 94. Adjudication of creditor claims is thus consolidated by statute in a single forum. No similar provision exists in the Bank Board's statutes to protect FSLIC receiverships from defending claims in courts around the country. By failing to include in the HOLA any express provision for judicial adjudication of creditor claims and by also leaving out the protective venue provisions of the NBA, Congress deliberately chose a different system for Bank Board-supervised receiverships. Congress clearly delegated to the Bank Board the task of devising a system for deciding and consolidating creditor claims in a single forum.

[9] The Comptroller currently takes no role in claims determinations, however.

The NCUA's statutory authority is particularly enlightening to this case. The Federal Credit Union Act ("FCUA") provided that a liquidating agent for a federal credit union "shall have power and authority, subject to the control and supervision of the Board and under such rules and regulations as the Board may prescribe, . . . to receive, examine, and pass upon all claims against the Federal credit union in liquidation." 12 U.S.C. § 1766(b)(3)(B). The Ninth Circuit in *Morrison-Knudson Co., Inc. v. CHG Intl, Inc.*, 811 F.2d 1209 (9th Cir. 1987), indicated that this language could be read to provide expressly for adjudication. *Morrison-Knudsen*, 811 F.2d at 1219 n.3. The Competitive Equality Banking Act ("CEBA"), enacted on August 10, 1987, amended the FCUA to provide NCUA-appointed liquidators for state chartered credit unions powers to adjudicate claims of creditors. The amendment is worded almost exactly the same as Section 1464(d)(6)(C). 12 U.S.C. § 1787(a)(1)(B).[10] The Congress stated the following purposes in enacting these amendments:

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[10] Except as otherwise provided in this subparagraph, no court may take any action for or toward the removal of any liquidating agent or, except at the instance of the [National Credit Union Administration] Board, restrain or affect the exercise of powers or functions of a liquidating agent.

12 U.S.C. § 1787(a)(1)(B).

The description of the National Credit Union Administration Board's liquidator's functions was also amended to mirror Section 1729(d):

> In connection with the liquidation of any insured credit union, the Board shall have the power to carry on the business of and collect all obligations to the credit union, to settle, compromise, or release claims in favor of or against the credit union, and to do all other things that may be necessary in connection therewith, subject only to the regulation of the Board, or, in cases where the Board has been appointed liquidating agent solely by a public authority having jurisdiction over the matter other than said Board, subject only to the regulation of such public authority.

12 U.S.C. § 1787(j).

> The Committee expects that liquidations conducted under this section *shall be accomplished as expeditiously as possible in order to achieve minimal disruption to the financial system.* Creditor, member and other claimants must be dealt with in a fair manner. These amendments clarify the [National Credit Union Administration's] authority to adjudicate liquidation claims. Upon final agency action, a claimant may seek recourse in court under the provisions of the Administrative Procedure Act.

S. Rep. No. 100-19, 100th Cong., 1st Sess. 25, *reprinted in* 8 U.S. Cong. News 489, 515 (Oct. 1987) (emphasis added).

This recent statement of the Congress also emphasizes the need for powers to resolve creditor claims expeditiously, in order to avoid "disruption" to the financial system. The language is thus a strong indication that Congress, which was undertaking a major overhaul of many banking statutes in the CEBA, presumed that the Bank Board's powers would be similarly interpreted.

V. There Is no Serious Question That FSLIC Has Exclusive Authority to Decide Claims Against the Receiverships That It Operates.

There is no serious question that claimants against FSLIC receiverships should be required to exhaust the administrative claims process. The Bank Board has broad authority to establish regulations to allow liquidation of failed thrifts "in an orderly manner." 12 U.S.C. § 1729(c)(3)(B). The Ninth Circuit found in *Morrison-Knudsen*, 811 F.2d at 1223, that the FSLIC's "interest in applying its expertise, correcting its own errors, making a proper record, and maintaining an efficient, independent administrative system" justifies imposing an exhaustion requirement in particular cases. Even Petitioner points out,

> FSLIC has the right in the first instance to decide whether to pay or refuse to pay a claim; and the Board can overrule FSLIC's decision just as the management of an insurance company can overrule the decisions of a claims adjuster. However, if the ultimate administrative decision is not to pay, the resulting dispute must then be resolved by the courts.

Petitioner's Brief ("Pet. Br.") at 26.

The purposes of an exhaustion requirement will be in large part unaccomplished, however, if claimants can, as the Ninth Circuit suggests in *Morrison-Knudsen*, repeatedly contest the need to exhaust in judicial proceedings. The result of that court's approach would be scores of costly legal battles in the courts over the need to exhaust, which will deplete the already insolvent receivership estates.

Moreover, because, as we argue *supra* p. 9, the exhaustion requirement is clearly a jurisdictional prerequisite to suit, there can be no exception. The Bank Board has established a mandatory scheme for FSLIC, as receiver, to review, allow and disallow claims. Valid regulations have been in place for 47 years. *See Morrison-Knudsen*, 811 F.2d at 1217 (recognizing validity of receivership claims regulations). These regulations have the force and effect of law. *de la Cuesta*, 458 U.S. 141, 153-154 (1982), *Milberg v. Lawrence Cedarhurst Federal Savings and Loan Ass'n*, 496 F.2d 523, 524 (2d Cir. 1974). The HOLA, 12 U.S.C. § 1464(d)(6)(C), clearly prohibits any interference by the courts with such functions of the receiver. Accordingly, no court may entertain claims against the receivership prior to administrative exhaustion. *Lyons Savings and Loan Ass'n*, 828 F.2d at 395; *Hudspeth*, 756 F.2d at 1103.

VI. Petitioner and the Amici Curiae for Petitioner Have Presented no Compelling Arguments in Opposition to the Conclusion That the FSLIC Has Exclusive Authority to Adjudicate Claims in the First Instance.

Petitioner argues that Section 1464(d)(6)(C) provides no authority for the conclusion that the FSLIC has exclusive authority to adjudicate claims in the first instance. According to Petitioner, Section 1464(d)(6)(C) must either be interpreted as permitting judicial adjudication of claims in the first instance or, alternatively, as a complete prohibition on judicial review, including APA review of administrative determinations. Amicus League also argues that FSLIC's reliance on Section 1464(d)(6)(C) "would mean that Congress intended to delegate to the discretion of the FSLIC as receiver authority to determine claims that is completely unreviewable." (Amicus League Br. at 23). We disagree. Absent specific congressional direction, there is a strong presumption that agency action is subject to judicial review. *See Traynor* v. *Turnage*, —— U.S. ——, 108 S.Ct. 1372, 1378 (1988); *Bowen v. Michigan Academy of Family Physicians*, 476 U.S. 667, 670 (1986). By Section 1464(d)(6)(C), Congress intended to prohibit judicial determination of claims in the first instance, because such adjudications would have the greater tendency to "restrain or affect" the receiver; but there is nothing in the language of the section to suggest that Congress intended to disrupt the courts' long standing jurisdiction to review final agency determinations under the APA. This conclusion is strengthened by the similar schemes applicable in other liquidations and the absence of any system where a receiver's or liquidator's decision is wholly unreviewable in court.

Petitioner and the Amicus League also rely on the power of the FSLIC to "sue and be sued", 12 U.S.C. § 1725(c)(4), as well as the NHA's three year limitation on depositor actions against FSLIC, 12 U.S.C. § 1728(c), as authority for the proposition that the FSLIC lacks exclusive jurisdiction. Unfortunately, Petitioner and the

Amicus League have failed to comprehend the dictinctions between FSLIC's corporate and receivership capacities and in so doing, have relied upon provisions that are inapposite to the issues presented to this Court. There is nothing to suggest that Congress intended these statutes to apply to FSLIC in its capacity as receiver. Rather, it is clear that the "sue and be sued" authority refers to FSLIC's corporate capacity. In its receivership capacity, FSLIC is subject only to the jurisdiction of the Bank Board or other appropriate state authority. 12 U.S.C. § 1729(d). Similarly, with respect to 12 U.S.C. § 1728(c), FSLIC makes insurance coverage determinations only in its corporate capacity. Section 1464(d)(6)(C)'s prohibition against restraints on receivership functions clearly does not apply to FSLIC in its corporate capacity as insurer of deposits.

Petitioner also argues that 12 U.S.C. § 1730(k)(1), which "was intended to keep certain actions in state courts, indicates what type of suits Congress expected to defend against in state courts" and by implication the type of suits Congress intended FSLIC to defend in federal court. (Pet. Br. at 27). Again, Petitioner's reference is misplaced. Section 1730(k)(1) merely allocates jurisdiction between state and federal courts. It is not an independent grant of jurisdiction.

Moreover, the Section 1730(k)(1) proviso accomplishes with respect to state-supervised receiverships what Section 1464(d)(6)(C) accomplishes with respect to Bank Board-supervised receiverships.[11] Both Section 1730(k)(1) and

[11] Section1730(k)(1) provides: "[A]ny action, suit, or proceeding to which the Corporation is a party in its capacity as conservator, receiver, or other legal custodian of an insured State-chartered institution and which involves only the rights or obligations of investors, creditors, stockholders, and such institution under State law shall not be deemed to arise under the laws of the United States. No attachment or execution shall be issued against the Corporation or its property before final judgment in any action, suit, or proceeding in any court of any State or of the United States or any territory, or any other court." 12 U.S.C. § 1730(k)(1).

Section 1464(d)(6)(C) were passed in 1966 as part of the same amendments to the Bank Board's and FSLIC's statutory schemes. Both sections have the effect of consolidating claims against the receivership estate, *i.e.*, claims by "investors, creditors and stockholders," in the courts or other authorities overseeing the receiverships. Both sections are also consistent with Section 1729(d), which centralized "regulation" of claims functions under the authority of the Bank Board or, if a state-appointed receiver, under the appropriate state authority, whether administrative or judicial.

Amicus League argues that "modern principles of judicial economy and evenhandedness are sacrificed" by what Amicus League views as the risk of a bifurcated process whereby the FSLIC would proceed in court for determination of liabilities and enforcement, while its party opponents would simultaneously be relegated to the administrative track for resolution of their disputes. (Amicus League Br. at 7). Both Petitioner and Amicus Watson make a similar argument (Pet. Br. at 29, n.23; Amicus Watson Br. at 8-10) in which they hypothesize that requiring that claims against insured thrifts follow an administrative track will likely result in a possibility of a single controversy, arising out of the same set of operative facts, being subject to simultaneous proceedings in two forums.

Petitioner and the Amici misunderstand the regulatory scheme at issue here. By creating an administrative track whereby FSLIC has exclusive authority to adjudicate claims against failed institutions in the first instance, Congress has provided a mechanism for speedy identification of those with valid claims against receivership assets. Where the switching of counterclaims against the receiver to the administrative track could result in parallel consideration of the same facts or issues, one forum or the

other may stay its proceedings pending completion of the other.[12] The claimant can always request expedited consideration in the claims process to avoid problems in defending against FSLIC in court. 53 Fed. Reg. 13105, 13112 (1988). In any event, the Bank Board has concluded that the benefits of consolidating claims against the estate outweigh the burden of possibly re-litigating some issues in suits brought by the receiver. Given the fact that most, if not all, other liquidation schemes also consolidate claims determinations, this is hardly an unreasonable conclusion.

Finally, Amicus League's reliance on *Riehle v. Margolies*, 279 U.S. 218 (1929), *Morris v. Jones*, 329 U.S. 545 (1947), and *Grant v. Buckner*, 172 U.S. 232 (1898), is also misplaced. Amicus League relies on these cases for the proposition that "courts traditionally have determined the validity of disputed claims without restraining or affecting a receivership." (Amicus League Br. at 22). In our view, such cases are not relevant because they all involved receivership systems quite different from the one at issue. As the Court made clear in *Morris*, 329 U.S. at 553, nothing prohibits a procedure for statutory receivers to decide claims, "except as such procedure collides with the Federal Constitution or Act of Congress." [13] (Citation omitted).

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[12]Most counterclaims are severable from the main action, however. *See, e.g., FSLIC v. Ziegler*, 680 F. Supp. 235, 238 (E.D. La. 1988), where the court concluded that, despite the characterization of its claim as an affirmative defense, Defendant Ziegler had "come forward with no evidence that it is anything other than a separate claim for compensation, which under *Hudspeth*, must first be submitted to the FHLBB, with review available under the Administrative Procedure Act."

[13] Because *Morris* involved a state scheme, it was held to "collide" with the Full Faith and Credit Clause. U.S. Const. art. IV § 1. FSLIC's scheme involves no such infirmity. *Id.*

VII. The Statutory Scheme Created for Resolution of Claims Against Failed Savings and Loan Associations Does Not Violate the United States Constitution.

A. *The Constitutional Arguments Raised By Petitioner Are Not Ripe for Resolution.*

Because Petitioner cannot show that it will suffer immediate and direct injury unless the Court reaches constitutional issues, its claims are not ripe for resolution by the Court at this time. *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 138 (1974); *Liverpool, New York & Philadelphia Steam-Ship Co. v. Commissioners of Emigration*, 113 U.S. 33, 39 (1885) (the Court "is bound . . . never to anticipate a question of constitutional law in advance of the necessity of deciding it"). " 'The Party who invokes the power [to annul legislation on grounds of its unconstitutionality] must be able to show not only that the statute is invalid, but that he has sustained or is immediately in danger of sustaining some direct injury as the result of its enforcement . . . .' " *Poe v. Ullman*, 367 U.S. 497, 504-505 (1961), quoting *Massachusetts v. Mellon*, 262 U.S. 447, 488 (1923) (brackets in original). *See also Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1020 (1984), where the Supreme Court held that a challenge on Article III grounds to a statutorily-mandated arbitration system was not ripe until an arbitrator had issued an award. The rationale for requiring exhaustion is that until appellees have been injured, there is no "case" or "controversy." The doctrines of finality and ripeness counsel courts to defer ruling on constitutional questions until completion of the administrative process. As the Supreme Court reasoned in *FTC v. Standard Oil Co.*, 449 U.S. 232, 242 (1980):

> Judicial intervention into the agency process denies the agency an opportunity to correct its own mistakes and to apply its expertise. Intervention also leads to piecemeal review which at the least is inefficient and upon completion of the agency process might prove to have been unnecessary.

(Citations omitted).

Courts should avoid entangling themselves in abstract disagreements over agency policies and should protect administrative agencies from judicial intervention until administrative results are final and have concrete effects upon the parties. *Abbott Laboratories v. Gardner*, 387 U.S. 136, 148-49 (1967).

Because Petitioner has not yet completed the claims procedure, it cannot show that it has sustained any direct injury as a result of having to pursue the process. In fact, Petitioner may receive full satisfaction of its claims without resort to the judicial process. That being the case, its constitutional challenge is not yet ripe. *See Aircraft & Diesel Equipment Corp. v. Hirsch*, 331 U.S. 752, 772-773 (1947) (possibility that claims will be decided favorably without resort to constitutional challenge to process makes the constitutional challenge unripe).

Finally, it is well settled that Petitioner must exhaust the administrative process even for challenges to the administrative process itself. *See, e.g., Hirsch*, 331 U.S. at 752. As the Seventh Circuit has recognized, "[s]o long as effective means for judicial review are ultimately available where the constitutional claims can be raised, appellant may not dispense with the requirement of prior administrative review, otherwise judicial review would be an abstract process." *Gaunce v. DeVincentis*, 708 F.2d 1290, 1293 (7th Cir.), *cert. denied*, 464 U.S. 978 (1983). *See also Weinberger v. Salfi*, 422 U.S. 749, 762 (1975).

B. *FSLIC's Receivership Claims Process Does Not Violate Article III of the United States Constitution.*

Article III, Section 1 of the United States Constitution provides that the judicial power of the United States shall be exercised by judges with tenure and protected from diminution of their salaries. U.S. Const. art. III, § 1. FSLIC is not staffed by "judges" with tenure and salary protection and therefore is not an Article III court. Nevertheless, the constitutionality of a delegation of decision making authority to a non-Article III tribunal does not turn on conclusory deference to the language of the Constitution. "Rather, the constitutionality of a given congressional delegation . . . must be assessed by reference to the purposes underlying the requirements of Article III." *CFTC v. Schor*, 478 U.S. 833, 106 S. Ct. 3245, 3256 (1986).

The preliminary administrative resolution of claims against the assets of a failed institution clearly does not violate Article III of the United States Constitution. As the Court has held, "Article III does not confer on litigants an absolute right to plenary consideration of every nature of claim by an Article III court." *Schor*, 106 S. Ct. at 3256. Instead, "the constitutionality of a given congressional delegation . . . must be assessed by reference to the purposes underlying the requirements of Article III." *Id.* The administrative determination of receivership claims is an essential part of a complex regulatory scheme in which there is a unique federal interest. Moreover, the rights at issue with respect to such claims are public rights, and the essential attributes of judicial power are retained in federal courts. In fact "[m]any matters that involve the application of legal standards to facts and affect private interests are routinely decided by agency action with limited or no review by Article III courts." *Thomas v. Union Carbide Agricultural Products Co.*, 473 U.S. 568, 583 (1985).

The Supreme Court has considered the constitutionality of delegations of judicial power several times in recent years and provided substantial guidance on the scope of the Article III requirements. In *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), the Court ruled unconstitutional a bankruptcy court's adjudication of a state law contract action by a debtor against a third party not otherwise subject to the bankruptcy court's jurisdiction. While a plurality of the Court engaged in a broad discussion of Article III, the

Court's holding was substantially more narrow. (Rehnquist, J., concurring in the judgment). The holding of *Northern Pipeline* was only that Congress may not vest in the bankruptcy courts the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, where the adjudication was without consent of the litigants and subject to ordinary appellate review. *Id.* at 89-92.

More recently, in *Schor*, the Court held that the Commodity Futures Trading Commission ("CFTC") regulations permitting the agency to adjudicate state law counterclaims did not violate Article III. The Court adopted a pragmatic approach, requiring that the constitutionality of a congressional delegation of adjudicative authority "be assessed by reference to the purposes underlying the requirements of Article III." *Schor*, 106 S. Ct. at 3256. The Court reasoned that the CFTC dealt only with a particularized area of law, issued orders enforceable only by order of federal courts, was subject to judicial review of both its factual and legal findings, and could not exercise all ordinary powers of district courts. The Court further held that the congressional purposes in authorizing an administrative agency to adjudicate state law claims—efficiency—outweighed the interests in requiring such claims to be adjudicated in Article III courts. *Id.* at 3259-60.

Like the CFTC in *Schor* and unlike the bankruptcy judges in *Northern Pipeline*, FSLIC and the Bank Board have no authority to preside over jury trials, issue writs of *habeas corpus*, or cite individuals for contempt. *Compare Schor*, 106 S. Ct. at 3259, with *Northern Pipeline*, 458 U.S. at 85. FSLIC and the Bank Board have no power to compel process or issue any kind of order. Like the CFTC, and unlike bankruptcy judges, FSLIC and the Board have no power to enforce determinations upon other parties. *Compare Schor*, 106 S. Ct. at 3259, with *Northern Pipeline*, 458 U.S. at 85. FSLIC as receiver

merely has the limited power to withhold payment from the estate. Pursuant to the APA, review of Bank Board decisions of law would be *de novo*, and review of findings of fact would be subject to the "arbitrary and capricious" standard of review. In our view this standard is fully adequate to preserve the essential role of Article III courts. *See* Fallon, *Of Legislative Courts, Administrative Agencies, and Article III*, 101 Harv. L. Rev. 915, 976-991 (1988).

Other than the power to decide claims in the first instance, under the FSLIC scheme, all attributes of judicial power remain in Article III courts. This scheme is not unique, but is consistent with other federal agencies empowered to adjudicate issues within their area of expertise, such as the National Labor Relations Board, the Social Security Administration, the Federal Trade Commission and dozens of other agencies that perform adjudication functions subject to judicial review under the APA. For these reasons alone, the FSLIC administrative claims process withstands Article III scrutiny.

In addition, the federal government indisputably has a unique and critical interest in maintaining public confidence in the savings and loan industry. To further that interest, Congress created the Bank Board and FSLIC to regulate and supervise all aspects of the savings and loan industry.

This Court recognized in *Union Carbide* that where the claims adjudication process was "an integral part of a program safeguarding the public health," the rights being adjudicated were, at least partly, in the nature of public rights. *Union Carbide*, 473 U.S. at 589. The safety and soundness of the nation's banking system is no less an important government interest than the public health and the receivership claims process is similarly an "integral part" of the regulatory scheme to preserve the health of the system. Accordingly the rights being adjudicated,

like those at issue in *Union Carbide*, need not be initially routed to an Article III forum.

To summarize, because Article III courts retain the essential attributes of judicial power over receivership claims, because the disputes delegated to FSLIC for initial adjudication are of the kind that need not be directed to an Article III court, and because Congress had weighty reasons for giving FSLIC adjudicatory power, the administrative claims process is fully consistent with Article III.

C. *FSLIC's Receivership Claims Process Does Not Violate the Seventh Amendment to the United States Constitution.*

The Seventh Amendment right to jury trial does not bar FSLIC adjudication of claims in the first instance. As this Court has stated repeatedly, "there is little or no basis for concluding that the Amendment should . . . be interpreted to provide an impenetrable barrier to administrative factfinding under *otherwise valid* federal regulatory statutes." *Atlas Roofing Co., Inc. v. Occupational Safety and Health Review Comm'n*, 430 U.S. 442, 460 (1977) (emphasis added). *See also Curtis v. Loether*, 415 U.S. 189, 194 (1974) ("[T]he Seventh Amendment is generally inapplicable in administrative proceedings, where jury trials would be incompatible with the whole concept of administrative adjudication and would substantially interfere with the [agency's] role in the statutory scheme") (footnote omitted).

Where Congress validly delegates authority to adjudicate claims to an administrative agency, such as in the FSLIC scheme, the Seventh Amendment does not bar that delegation even though the trial right might have applied had Congress left authority to adjudicate those claims with the courts. *Pernell v. Southall Realty*, 416 U.S. 363, 383 (1974), explaining *Block v. Hirsch*, 256 U.S. 135, 158 (1921).

Moreover, in order to prevail on a Seventh Amendment right to jury trial challenge, the action at issue must be the type that would have been tried in courts of law, rather than courts of equity or admiralty at the time the Seventh Amendment was adopted. *Atlas Roofing*, 430 U.S. at 449. Claims raising equitable issues or seeking equitable relief do not give rise to the jury trial right. *Id.*; *Katchen*, 382 U.S. at 336-338. Because Petitioner's claims against FirstSouth assets are now claims against the receivership estate of a FSLIC liquidating receiver, they are in the nature of claims against a bankrupt estate. This Court has held that claims against a bankrupt estate sound in equity not in the common law, and that therefore the right to jury trial is inapplicable. *See Katchen*, 382 U.S. at 336; *Barton v. Barbour*, 104 U.S. 126, 134 (1881) ("a claim of a debt or damages against the bankrupt is investigated by chancery methods"). The Court has explained that even if a claimant against a bankruptcy estate might otherwise be entitled to a jury trial, "when the same issue arises as part of the process of allowance and disallowance of claims, it is triable in equity. The Bankruptcy Act, passed * * * to establish uniform laws on the subject of bankruptcy, converts the creditor's legal claim into an equitable claim to a pro rata share of the *res* . . . ." *Katchen*, 382 U.S. at 336.

The HOLA and NHA statutes serve the same function as the old Bankruptcy Act. They create an orderly process for the allowance and disallowance of claims against an insolvent institution, so that *pro rata* shares of the receivership estate may be determined. *Cf. Barton*, 104 U.S. at 134 ("Very analogous to the case of an assignee in bankruptcy is that of a receiver of an insolvent railroad company or other corporation"). Thus, they too convert legal claims into equitable ones. Accordingly, FSLIC, like the bankruptcy courts under the old Bankruptcy Act, need not provide a jury trial when performing its claims determination function.

D. *FSLIC's Receivership Claims Process Does Not Violate the Due Process Clause of the Fourteenth Amendment to the United States Constitution.*

Petitioner argues that the FSLIC's adjudicatory scheme deprives potential claimants of due process, because of FSLIC's dual function of insurer and liquidator. As insurer, FSLIC reimburses the depositors of the defaulting savings and loan and becomes subrogated to their claims against the receivership estate. As liquidator, FSLIC marshals the savings and loan's assets and pays valid credit obligations according to the list of priorities and to the extent of available assets. The fewer claims that ultimately are allowed, the more money that FSLIC is able to recoup as subrogee to the depositors' claims. This syllogism creates what Petitioner views as an inherent conflict of interest in violation of due process.

Congress has charged FSLIC and the Bank Board with the responsibility of maintaining the financial stability of the savings and loan industry. Accordingly, FSLIC and the Bank Board have a strong interest in fostering public confidence in the fairness of liquidation proceedings in order to maintain the public's faith in the savings and loan industry and its regulators. There is no reason to think that in carrying out the receivership role Congress assigned it, FSLIC will do anything other than give "due consideration to the interest of all of the claimants upon the assets of the association." S. Rep. No. 90-1263, 90th Cong., 2d Sess. 10, *reprinted in* 1968 U.S. Code Cong. & Admin. News 2530, 2539; *see also Womble v. Dixon*, 752 F.2d 80, 81 (4th Cir. 1984) (even if a conflict between FSLIC's dual roles does exist, there is no reason to assume "that the FSLIC will not carry out its statutory duties").

Moreover, FSLIC's role as insurer is completely separate from FSLIC's role as receiver. Even with respect to the same defaulting institution, there is no overlap between FSLIC's insurance personnel and FSLIC's receivership personnel. Furthermore, the remuneration of those

who evaluate claims is fixed. These personnel have no incentive to disallow claims that otherwise would reduce the funds available to FSLIC as subrogee. This lack of a personal stake was important in this Court's analysis of the child labor enforcement provision of the Fair Labor Standards Act upheld against a due process challenge in *Marshall v. Jerrico, Inc.*, 446 U.S. 238 (1980). Here, as in *Jerrico*, the possibility of inherent bias is minimized by the absence of incentives for FSLIC adjudicators to deny claims unjustly.

FSLIC's dual functions are not unique in administrative law. The Social Security Administration ("SSA") adjudicates disputes involving direct disbursements from various insurance trust funds it administers. SSA's interest in the outcome is analogous to FSLIC's because SSA too has conflicting responsibilities to conserve the trust funds, but also to pay valid claims. Indeed, the "conflict" in FSLIC's dual role is less significant than SSA's because FSLIC in its corporate capacity is merely a competing creditor, not the guardian of the receivership funds. It is only in its entirely separate receivership capacity that FSLIC exercises this latter function.

This Court has repeatedly stressed that the challenger's burden to establish a *per se* due process violation is a heavy one. There is a "strong presumption in favor of the validity of congressional action" in light of the Court's recognition of the " 'congressional solicitude for fair procedure . . . .' " *Schweiker v. McClure*, 456 U.S. 188, 200 (1982), quoting *Califano v. Yamasaki*, 442 U.S. 682, 693 (1979). Furthermore, agencies are entitled to a presumption "that they will act properly and according to law." *FCC v. Schreiber*, 381 U.S. 279, 296 (1965). As the Court said in dismissing a due process challenge to the Bank Board's dual roles of appointing conservators and presiding over hearings to determine whether the conservators were properly appointed, it is inappropriate for courts to "assume in advance that an administrative hear-

ing may not be fairly conducted." *Fahey v. Mallone*, 332 U.S. 245, 256 (1947).

In view of the foregoing, it must be concluded that Petitioner has failed to demonstrate that FSLIC's administrative claims process violates due process laws.

CONCLUSION

The National Council believes that the Bank Board and FSLIC have authority to promulgate regulations for apportioning assets of institutions in receivership, and that these procedures are subject to judicial review under the APA. They provide an opportunity for claimants to receive a determination of their claims, while conserving assets of the failed institution. These procedures further the purposes of Congress as expressed in the HOLA and NHA, and they are in the best interest of the thrift industry.

Respectfully submitted,

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APPENDICES

APPENDIX A

USL

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January 30, 1986

Director, Information Services Section
Office of the Secretariat
Federal Home Loan Bank Board
1700 G Street, N.W.
Washington, D.C. 20552

RE: Resolution No. 85-1007

Dear Sir:

We congratulate the Board in its efforts to clarify and streamline its regulations governing the appointment and powers of conservators and receivers. We are appreciative of the Board's concern that it be able to act in a timely fashion before the assets of an ailing association are dissipated and of the need to generally maintain the priority of the FSLIC as a creditor over other parties

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* The U.S. League of Savings Institutions, serves the more than 3,500 member institutions which make up the $1.1 trillion savings association and savings bank businesses. League membership includes all types of institutions—federal and state-chartered, stock and mutual. The principal officers include: Gerald J. Levy, Chairman, Milwaukee, Wisconsin; Joe C. Morris, Vice Chairman, Emporia, Kansas; William B. O'Connell, President, Chicago, Illinois; Philip Gasteyer, Executive Vice President and Director of Washington Operations; and Rita I. Fair, Senior Vice President, Regulatory Operations. League headquarters are at 111 East Wacker Drive, Chicago, Illinois 60601. The Washington office is located at 1709 New York Avenue, N.W., Washington, D.C. 20006. Telephone: (202) 637-8900.

who have dealt with the association because of the overwhelming public necessity of maintaining the integrity of the FSLIC fund. The U.S. League recognizes that some of these proposals may, in particular instances, impose a hardship on some of its member institutions or those who deal with one of those institutions. We nevertheless generally support the Board's regulations because of the overriding public need to protect the FSLIC fund. We recognize that it is important to give the FSLIC the broad power it needs to protect the fund and to maintain public confidence in the financial institution community. However, we believe that some provisions may be counterproductive and may erode public confidence in savings institutions and their ability to effectively compete in the marketplace. This is particularly true in secondary market activities and in areas where associations are selling securities chiefly through finance subsidiaries in instances where the protections afforded to the FSLIC may make it impossible for associations to deal in the broader securities and secondary mortgage markets because of the lack of certainty as to whether their contracts will be honored in the event of receivership.

The secondary market and securities activities are particularly sensitive because the holders of mortgage participations or mortgage-backed securities have no direct knowledge of the institution and should not be held accountable for what may subsequently happen to the institution.

We also are concerned that the rights of all shareholders to contest the appointment of a receiver be recognized so that the extensive flow of capital into associations which has occurred in the last three years through mutual stock conversions will not be jeopardized. The Board has actually encouraged conversion from mutual to capital stock because such conversion provides a cushion to the Federal Home Loan Bank Board and, thus, helps protect the insurance fund. To the extent the regulations ignore the rights of minority shareholders, they may be jeopardizing the inflow of capital into institutions.

Our specific comments as to the regulations are as follows:

(1) *Finance Subsidiaries*

The regulations should specifically state that the finance subsidiary of an institution which is put into receivership will remain separate and will not be considered an asset of the receivership nor will the FSLIC void transactions of the finance subsidiary. This is the essence of the FHLBB General Counsel opinion dated March 23, 1984. However, the General Counsel's opinion was a little nebulous in that it stated "a court would not uphold the receiver's attempt to disregard the separateness of the subsidiary". We would hope that the FHLBB would go further and specifically state that the receiver would not attempt to disregard the separateness of the subsidiary, assuming that the finance subsidiary regulations were complied with.

(2) *Secondary Market Considerations, 569c.10.*

We are very appreciative of the Board's codification of the general rule characterizing loan participations as true sales and not as creating a debtor-creditor relationship. As the Board noted in its comments the Bankruptcy Law of 1978 contains specific provisions to deal with the *Hamilton Mortgage Company* case. The committee report to that statute specifically said: "Section 541(e) makes clear that the seller's retention of the mortgage documents and the purchaser's decision not to record do not impair the asset sale character of secondary mortgage market transactions. The committee notes that in secondary mortgage market transactions the parties may characterize their relationship as one of trust, agency, or independent contractor. The characterization adopted

by the parties should not affect the statutes in bankruptcy of *bona fide* secondary mortgage market purchases and sales."

It would indeed be an anomaly if associations were better protected dealing with institutions which were subject to the Bankruptcy law rather than savings institutions which are subject to the receivership and conservator provisions of the FHLBB.

However, as the Board noted, there have been decisions involving the FDIC where even though the sale nature of the participation interest was noted, the participation holder had his rights extinguished by the original borrower's right of offset.

Such a right of offset would work as follows. Assume a borrower has borrowed $500,000 from the savings institution. The savings institution then sells one-half of that interest to a third party in the secondary market. The borrower then makes a $500,000 deposit with the institution and the institution goes into receivership. As the Board itself notes, some courts have allowed the borrower to offset his mortgage note with the savings deposit which could leave the buyer of the participation interest in such a case with nothing. In a situation where, for example, the borrower had a $500,000 savings deposit, he would be able to offset that against the $500,000 note so that the entire debt would be extinguished. The third party which has bought half of that note, however, is not aware of any of these other transactions. It has bought for good value one-half the interest of the note and has presumed it would be entitled to one-half the payments. It now finds out that the debt has been extinguished. In the *Mademoiselle* case, discussed by the Board, the court refused to allow the third party purchaser the right to have a preferred claim to its share of the offset. If the FHLBB does not grant such third party purchasers the right to a preferred

claim to their share of offset, there will be continuing uncertainty in the secondary market as to what the purchaser is really buying. Even warranties made at the time of sale regarding deposits of the noteholder would be of no value since the noteholder could put a deposit in at a subsequent time.

We agree with the Board that sales with recourse would change the nature of the transaction from a sale to more of a financing and thus should not be treated as a true sale. However, in this regard, the regulation should be clarified to insure that the recourse which is being referred to is the "recourse" as defined under the FHLBB regulation 561.8 (12 C.F.R. 561.8).

We also congratulate the Board for stating that where the association sells 100% interest in a loan but retains legal title to supervise or service the loan, the loan does not become property of the estate unless the association also retains equitable title. So that, where the association has retained legal title only for the purpose of servicing, the equitable interest in the property will not be considered an asset of receivership.

In this regard, however, we are concerned that the Board's proposed SEC 569c.5 which would prevent parties from attempting to enforce certain participation agreements. Many participation agreements, including the U.S. League's illustrative participation agreements, provide for the largest participation holder to succeed to the rights and titles of the seller regarding the servicing of the loans and to exercise those powers in the event the seller becomes insolvent or a receiver is appointed. Such provisions are needed to assure the participation holders that payments will not be in the receivership proceedings, particularly as to the servicing aspects of the loan. In this regard, we must remember that while the FSLIC has a strong public interest to assure the safety of the fund, in its zeal to do so it may have just

the opposite effect. Associations which most need to avail themselves of the flexibility of the secondary market and new financing techniques may be in fact denied access to markets because of third party fears that the association will become insolvent and the payment streams will be tied up in receivership proceedings.

Authorization to Contest Receivership Appointment, 569a.8

The proposed regulations state that the appointment of a receiver can only be contested by authorization of the board of directors. We are deeply concerned that this will result in the freeze-out of minority shareholders which may very well have interests separate from the interests of the majority shareholders. Since the appointment of the receivership may, as a practical matter, result in the total extinguishment of their investment in the institution, they should have the right to contest the appointment of the receiver even if the board of directors does not do so. To freeze-out minority shareholders in this manner will have just the opposite effect the Board intended, as it may limit the flow of capital into institutions if they realize that the rights of capital stockholders will be so easily disregarded and thus increase the exposure of the FSLIC fund.

Management Contracts, (563.39(a))

We agree with the Board that there have been instances where associations may have acted improperly by providing for excessive bonuses upon the appointment of a conservator or receiver. We do not object to the Board's providing that there should not be a bonus, severance pay or other compensation related to the appointment of a receiver or conservator as such. However, we strongly disagree that employment contracts entered into before the appointment of a receiver would be automatically terminated. This would prevent those

associations which are most in need of professional managers from obtaining those managers since no professional manager would enter into an agreement with an association where there was a possibility within one or two years it might be in receivership and his employment contract would be ended. Employment contracts should be allowed to continue as in the case of other catastrophic events such as takeovers or mergers; there should be no difference.

Avoidability of Contracts, 569a.8

Contracts voided by the FSLIC should be restored if a court later finds the appointment invalid. The Board itself has stated that contracts entered into by the receivership cannot be voided even if the court finds that the receivership was invalid and the affairs should be turned back to the association. While we are not enthusiastic about the FHLBB's position that even where a receivership is subsequently declared invalid the contracts entered into by the FSLIC would nevertheless remain valid, we understand the need for the receiver to have public confidence when it enters into public contracts so that those contracts will be upheld. The same considerations of public confidence require the opposite conclusion where a receiver is invalidating existing contracts with the institution. This, in fact, undermines confidence and although we understand the Board's need to have this power, we believe that where the receivership is subsquently declared invalid, those contracts which were voided should be reinstated. We believe this would have a salutory effect in that it would act as a restraining force. It would also prevent the temptation to be too aggressive in appointing receivers to avoid existing contracts which may be just "bad deals". From a cynical point of view some observers might argue that the FSLIC could protect its fund by asserting receivership authority, voiding contracts which would remain

void even though it would subsequently be held that there were no grounds for receivership. Clearly, the Board would, in fact, not do this knowingly, but we believe it is important to maintain the public's perception of equity in this area. If such is indeed the perception, associations below or near regulatory net worth may indeed find it difficult to enter into any contracts where the FSLIC would theoretically have such an easy way out.

Prepayment Penalties, 569c.8d(2)

We frankly do not agree with the characterization of prepayment fees which may be in excess of the usual interest rate loss as "windfalls". These prepayment clauses are bargained for to avoid guessing games as to the precise nature of the damages. In essence, these are liquidated damages which are designed to avoid protracted litigation and uncertainty. To disregard this bargained for consideration and substitute instead actual damages would invite further uncertainty and represent a usurpation of the relevant contractual provisions. Again, we commend the Board for its comprehensive revision of the regulations and for its aggressive stance in trying to protect the integrity of the FSLIC fund and thus public confidence in all financial institutions. Thank you for this opportunity to comment.

Sincerely

/s/ Robert W. Bartlett
ROBERT W. BARTLETT
Senior Vice President and
Director of Technical Services

RWB/blk

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF FLORIDA
PENSACOLA DIVISION

PCA 86-04294 WEA

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION,
as Receiver for AUDUBON FEDERAL SAVINGS AND
LOAN ASSOCIATION,
Plaintiff,

vs.

J. W. URQUHART, JR., *et al.*,
Defendants.

MEMORANDUM DECISION

In October of 1985, Audubon Federal Savings and Loan Association (Audubon) instituted foreclosure proceedings on properties owned by J. W. Urquhart. Fairfax Savings Association (Fairfax) filed a complaint for declaratory relief and a motion to intervene, based upon a participation agreement between Audubon and Fairfax and alleging breach of that agreement by Audubon.

Audubon was declared insolvent by the Federal Home Loan Bank Board (FHLBB), and it appointed Federal Savings and Loan Insurance Corporation (FSLIC) as receiver. FSLIC substituted itself for Audubon, and successfully removed the proceedings to this court. FSLIC, relying upon *Northern Mississippi Savings & Loan v. Hudspeth*, 756 F.2d 1096 (5th Cir. 1985), *cert. denied*, —— U.S. ——, 106 S.Ct. 790, 88 L.Ed.2d 768 (1986), then moved for the dismissal of Fairfax pursuant to Federal Rules of Civil Procedure 12(b)(1) for lack of

jurisdiction. This court, following *Hudspeth*, granted that motion, holding that under 12 U.S.C. §§ 1729(d) and 1464(d)(6)(C) such claims must be resolved administratively pursuant to applicable federal regulations.

Fairfax has now moved this court to reconsider. Its motion presents a constitutional challenge based upon Article III and *Glen Ridge I Condominiums, Ltd. v. FSLIC*, No. 05-85-00873-CV, slip op. (Tex. Ct. App. December 30, 1986). Later, Fairfax provided this court with a copy of *Morrison-Knudsen Co. v. CHG International*, No. 86-2063, slip op. (9th Cir. Feb. 25, 1987), which is in direct opposition to the *Hudspeth* decision. FSLIC was given opportunity to respond to both *Glen Ridge* and *CHG*. It responded by providing a copy of appellees' motion for rehearing in *Glen Ridge*, a copy of FSLIC's petition for rehearing and suggestion of appropriateness of rehearing *en banc* in *CHG*, and copy of slip opinion in *Tamarind v. Twin Oaks*, No. 86-107-Civ.-Ft. M.-13(B).

This court, having considered the memoranda of both parties and the other authorities presented, denies the motion to reconsider for the reasons set out below.

Lack of Subject Matter Jurisdiction

In *North Mississippi Savings & Loan v. Hudspeth*, 756 F.2d 1096, 1101 (5th Cir. 1985), *cert. denied*, —— U.S. ——, 106 S.Ct. 790, 88 L.Ed.2d 768 (1986), the Fifth Circuit stated:

> In explaining the Bank Protection Act of 1968, which made § 1464(d)(6)(C) applicable in receiverships of state thrift institutions, the Senate confirmed that the FSLIC's authority "[i]n carrying out its receivership responsibilities . . . would be subject only to the regulation of the Federal Home Loan Bank Board. . . ." S.Rep. No. 1263, 90th Cong., 2d Sess. 10, *reprinted in* 1968 U.S.Code Cong. & Admin.News 2530, 2539. Congress wanted the FSLIC to be able to act quickly and decisively in reorganizing, operating, or dissolving a failed institution, and intended that the FSLIC's ability to accomplish these goals not be interfered with by other judicial or regulatory authorities.

To accomplish this end, disputes were relegated to the administrative process. The 9th Circuit, in *Morrison-Knudsen Co. v. CHG International*, No. 86-2063, slip op. (Fef. 25, 1987), looked at the statute and the regulations and fund that Congress did not intend the FSLIC to have the power to adjudicate claims and that the regulations overstepped the intent of Congress. Where the *Hudspeth* court found congressional intent that the FSLIC be subject only to the regulation of the FHLBB, the 9th Circuit, in *CHG*, found no such intention.

The 9th Circuit's approach was premised upon its belief that, had Congress so intended, it would have stated that intent in express terms, and because the statute nowhere expressly states the FSLIC is to have the authority to resolve the validity of a creditor's claims that authority does not exist. It is an equally valid form of analysis to state that, had Congress intended to withhold that authority, it would have expressly done so.

The problem then is to determine which analytical approach is proper in light of the statute being construed. This court believes the latter approach warranted in this instance.

12 U.S.C. § 1729(d) (1982 amendment) reads as follows:

> In connection with the liquidation of insured institutions, the Corporation shall have power to carry on the business of and to collect all obligations to the insured institutions, to settle, compromise, or release claims in favor of or against the insured institutions, and to do all other things that may be necessary in

connection therewith, subject only to the regulation of the Federal Home Loan Bank Board, or, in cases where the Corporation has been appointed conservator, receiver, or legal custodian solely by a public authority having jurisdiction over the matter other than said Board, subject only to the regulation of such public authority.

In view of the language of § 1729(d), and the restrictions embodied in § 1728(c) (regarding despositor claims), the proper conclusion to draw is that, if Congress did not place an express limitation upon the actions or powers of FSLIC, and the actions or powers involved are regulated by FHLBB, Congress intended that FSLIC have those powers.

The court, in *CHG*, believed it illogical that disputes regarding depositor claims were not removed from judicial determination and disputes regarding creditor claims were. This court finds logic in the distinction. The primary purpose of this entire statutory scheme was to protect the average depositor from financial ruin resulting from the failure of a savings institution. This purpose would be defeated by the denial of even one valid depositor claim. This legislation was not designed to protect creditors.

Under *Hudspeth*, all claims of Fairfax are switched to the administrative process by § 1464(d)(6)(C). Fairfax can challenge the FSLIC's actions before the FHLBB and, if dissatisfied, can seek judicial review under the Administrative Procedure Act. Until such time, the statute prevents Fairfax from going forward in any court before seeking review before the FHLBB. *See e.g., Sunrise Savings and Loan Assoc. v. Lir Development Co.*, 641 F.Supp. 744, 746 (S.D. Fla. 1986).

This court concludes that 12 U.S.C. §§ 1464, 1729(d), and 1728(c) preclude courts from adjudicating creditor claims and thus dismissal due to lack of subject matter jurisdiction is proper.

The Constitutional Challenge

Fairfax also pressed upon this court the holding of *Glen Ridge I Condominiums, Ltd. v. FSLIC*, No. 05-85-00873-CV, slip op. (Tex. Ct. App. December 30, 1986). In that case the court, relying upon *Northern Pipeline Co. v. Marathon Pipeline Co.*, 458 U.S. 50, 102 S.Ct. 2858, 73 L.Ed.2d 598 (1982), held that Congress had violated Article III in precluding judicial determination of creditor claims. The 9th Circuit, in *CHG*, also expressed its belief that if Congress had relegated such disputes to administrative procedure there were serious Article III implications.

The general rule is that no court should pass on the constitutionality of a federal statute if the case may be disposed of on other grounds. Here there may be other grounds as administrative proceedings have not been completed. However, both parties have, before this court, presented and briefed the constitutional issue. Because they have done so, this court will proceed to determine it.

In *Northern Pipeline* the Court held that final adjudicatory power granted bankruptcy courts by Congress violated Article III. In so holding the Court was troubled by the extensive powers given bankruptcy courts. The Court found that the contract dispute in that case was a private right and thus relegated to Article III courts. The private rights doctrine allows delegation of adjudicatory power to non Article III courts only when a public right is implicated. Public rights arise "between the Government and persons subject to its authority in connection with the performance of the constitutional function of the executive or legislative departments." *Northern Pipeline*, 458 U.S. at 65-66. A public right is not a liability of one individual to another.

The Court further held that "[W]hen Congress creates a statutory right, it clearly has the discretion . . . to provide that persons seeking to vindicate that right must do

so before particularized tribunals created to perform the specialized adjudicative tasks related to that right." *Id.* at 83. And, in *Thomas v. Union Carbide Agricultural Products*, 473 U.S. ——, 105 S.Ct. 3325, 87 L.Ed.2d 409 (1985), the Court stated that Congress may grant jurisdiction to a non-Article III body over disputes so closely integrated into a public regulatory scheme as to be a matter appropriate for agency determination with limited judicial involvement (review only) when the rights created seem private.

Finally, in *Commodity Futures Trading Commission v. Schor*, 478 U.S. ——, 106 S.Ct. 3245, 92 L.Ed.2d 675 (1986), the Court held that a "private right" counterclaim could be heard by a non-article III tribunal. 92 L.Ed.2d at 686. It held there are three factors to be weighed to determine whether an administrative determination violates Article III. They are: 1) the extent to which the 'essential attributes of judicial power' are reserved to Article III courts and, conversely, the extent to which the non Article III forum exercises the range of jurisdiction and powers normally vested only in Article III courts, 2) the origin and importance of the rights being adjudicated, and 3) the concerns that drove Congress to depart from Article III.

In applying the foregoing cases to the case at bar it is first noted that the power of the FSLIC and the FHLBB is not nearly as broad as the power of the bankruptcy court which so troubled the court in *Northern Pipeline*. Additionally, Fairfax would have no dispute with anyone but Audubon were it not for the congressional creation of FSLIC and the legislative creation of its standing as a party. Thus this entire action can and should be construed as a public right (*Northern Pipeline*) or at least one so closely integrated into a public regulatory scheme (*Union Carbide*) to be appropriate for agency determination. Further, in applying the *Commodity Futures* factors one finds that the FSLIC does not have powers akin to

those of Article III courts and that any forthcoming determination of it is reviewable by an Article III court, the original of any right Fairfax has to proceed against the FSLIC is statutory, and Congress wanted to facilitate prompt liquidation because delay can wreck havoc upon depositors.

As FSLIC points out, at least four federal court decisions have held that the determination of a state law claim by FSLIC as receiver does not violate Article III of the Constitution. *Baer v. Abel*, 637 F.Supp. 347 (W.D. Wash. 1986); *First Amer. Sav. Bank v. Westside Federal Sav.*, 639 F.Supp. 93 (W.D. Wash. 1986); *Lyons Sav. & Loan Ass'n v. Westside Bankcorp.*, 636 F.Supp. 576 (N.D. Ill, 1986); and *Rembold v. Gibralter Savings & Loan Ass'n*, 624 F.Supp. 1006 (W.D. Wash. 1985), overturned on other grounds No. 86-3658 (9th Cir. Feb. 25, 1987).

This court concludes the statutory scheme presented here is constitutional.

Order will be entered denying the motion for reconsideration.

DATED this 7 day of April, 1987.

/s/ Winston E. Arnow
WINSTON E. ARNOW
Senior Judge